



JOHN ENGLER  
GOVERNOR

DEPARTMENT OF EDUCATION  
LANSING



THOMAS D. WATKINS, JR.  
SUPERINTENDENT OF  
PUBLIC INSTRUCTION

March 7, 2002

**MEMORANDUM**

**TO** State Board of Education

**FROM** Thomas D. Watkins, Jr.

**SUBJECT** Interim Report: From Proposal A to Proposal A+

In August 2001 as a collective body by unanimous vote you asked me to conduct a review to answer the question, "How much will it take to fully fund public education in Michigan?" I am pleased to present the first draft of the Task Force's work. I would like to thank Dr. Neil Theobald from Indiana University for his expertise. Dr. Theobald conducted the interviews and created this report. I also acknowledge the generosity of North Central Regional Educational Laboratory (NCREL) for underwriting this research project. Finally, I thank the State Board of Education for their vision and willingness to review Proposal A. Their leadership provided the real impetus that initiated this report.

First, this should be viewed as a starting point. It is intended to be a stimulus for conversation, dialogue and debate among opinion leaders, policy makers and the general public. It is not intended to be a comprehensive or exhaustive list of options or solutions. It is intended to provoke innovative thinking that will enhance and improve the system of school finance in Michigan. Not all of the ideas or suggested options should be accepted at face value. Not all should be seen as sensible solutions but rather as a beginning point for discussion that will be the foundation for positive change.

The benefit of Proposal A is recognized. However, much like a 1994 automobile, Proposal A may be in need of an engine overhaul and body redesign to remain contemporary. Perhaps Proposal A was good in the 20<sup>th</sup> century. Now, perhaps the citizens and children of Michigan deserve Proposal A+ as we move into the 21<sup>st</sup> century. As policy makers, we have a responsibility to take a conscious look at our decisions to see if they withstand the test of time and to ask ourselves if we can do better. It is with that intent that I share this report. Our goal should be to work together to find a shared vision and common agenda that will address the shortcomings of the existing system.

KATHLEEN N. STRAUS - PRESIDENT • SHARON L. GIRE - VICE PRESIDENT  
MICHAEL DAVID WARREN, JR. - SECRETARY • EILEEN LAPPIN WEISER - TREASURER  
MARIANNE YARED MCQUIRE - NASBE DELEGATE • JOHN C. AUSTIN • HERBERT S. MOYER • SHARON A. WISE

608 WEST ALLEGAN STREET • P.O. BOX 30008 • LANSING, MICHIGAN 48909  
[www.michigan.gov](http://www.michigan.gov) • (517) 373-3324

Following your review this report will be shared with others including the Governor, gubernatorial candidates, legislature, education community, business and labor organizations, education reporters, general media and editorial writers. It will be posted on the department's website with a survey to collect feedback. We will hold several public forums throughout the State to gather input regarding how school funding, including operational, infrastructure and administrative efficiencies, has evolved since Proposal A was implemented.

I look forward to our discussion about this report. May it provide provocative food for thought and a starting point for productive dialogue that will lead to an optimal and improved school-funding model for all of Michigan's children?

# From Proposal A To Proposal A+

*A discussion of issues and options regarding the  
financial requirements of  
public education in Michigan*

A Report to the Michigan State Board of Education  
from  
Tom Watkins, Superintendent of Public Instruction  
and the  
School Finance Task Force

March 2002

## **School Finance Task Force**

**Mike Addonizio**, Associate Professor  
Educational Leadership and Policy Studies, Wayne State University

**David Arsen**, Professor  
Michigan State University

**Bill Bushaw**, Chief Academic Officer  
Michigan Department of Education

**Tom Clay**, Senior Research Associate  
Citizens Research Council of Michigan

**Julie Cullen**, Assistant Professor  
Department of Economics, University of Michigan

**Doug Drake**, Associate Director  
State Policy Center, Wayne State University

**Elisabeth Gerber**, Director  
Center for Local, State and Urban Policy (CLOSUP)  
University of Michigan

**Philip Kearney**, Professor Emeritus  
University of Michigan

**Sabrina Laine**, Associate Director  
Center for Internal Coordination and External Relations  
North Central Regional Educational Laboratory

**Elaine Madigan**, Director  
State Aid and School Finance, Michigan Department of Education

**David Olmstead**, Attorney at Law  
Thurn, Maatsch and Nordberg, P.C.

**David Plank**, Director  
The Education Policy Center, Michigan State University

**Earl Ryan**, Executive Director  
Citizens Research Council

**Neil Theobald**, Associate Professor of Educational Finance  
Indiana University

**Tom Watkins**, Superintendent of Public Instruction  
Michigan Department of Education

**Carol Weissert**, Director  
Institute for Public Policy and Social Science Research  
Michigan State University

**Carol Wolenberg**, Deputy Superintendent  
Michigan Department of Education

**Pam Wong**, Chief of Staff  
Michigan Department of Education

## Introduction

A cost-effective school funding system allocates resources towards achieving those goals that are most important to the state. The purpose of this report is to assist Michigan policymakers in ensuring that their school funding system continues to be closely tied to the evolving goals and aspirations they hold for the state's K-12 schools.

This process begins by asking policymakers to clearly identify:

- Problems to be resolved
- Goals to be achieved
- Conditions to be created

Only then can they infuse more data-driven decision making into their debates on the relative value of the funding options available to them. Currently, this process too often operates in the reverse direction. State policymakers are asked to weigh costly policy options (e.g., vouchers, early childhood education, annual standardized testing) *before* they have gone through the systematic analysis needed to answer the critical questions, “What are we trying to do here? What goals in our state do we most want a school funding solution to achieve? Do these proposals directly address our issues?” Issues must drive solutions.

The need for such an issues-driven school funding process is particularly important in a state such as Michigan that has moved to substantially expand its traditional role in funding K-12 education. In the 1993-94 school year, state revenues comprised 31% of Michigan school revenue; the next school year, state revenue comprised 79% of Michigan school revenue.<sup>1</sup> Under Proposal A, per-pupil spending in Michigan is about 20 percent above the national average with the state providing 80% of school revenue.<sup>2</sup> This substantial financial responsibility compels prudent state policymakers to continually update and enhance their understanding of Michigan's

---

<sup>1</sup> Kearney, C. P. (1994). *A primer on Michigan school finance*. Ann Arbor: University of Michigan, p. 4.

<sup>2</sup> National Education Association (2001). *Rankings of the state*. Washington, DC: Author, p. 42, 55.

system of school funding and to plan for improvements to a system that claims such a large share of state resources.

### **Background<sup>3</sup>**

#### *Revenue Generation*

In the fall of 1994, as a result of a legislative reform package and subsequent voter approval of a 2-percentage point increase in the general sales tax, Michigan's public schools began operating under an entirely new set of school finance arrangements. In prior years, under Michigan's Equal Yield Approach, local property taxes provided better than 60 percent of the revenues needed to fund the public schools. Furthermore, these taxes were levied only at the local level; the State did not levy property taxes for school purposes. Under the new foundation approach adopted by the Legislature in December 1993, three important changes came about.

First, property taxes for school purposes were substantially reduced. Beginning in 1994-95, property tax revenues provided only some 32 percent of K-12 operating funds as compared to 60 plus percent in 1993-94 and immediately prior years. Thus, taxpayers in most of Michigan's school districts witnessed a considerable reduction in property tax millage rates for school operations.

Second, rather than millage rates being applied uniformly on all property, different rates are applied to homestead and non-homestead property.<sup>4</sup> Homestead property is taxed at 6 mills, (referred to as State Education Tax or SET) non-homestead property at 18 mills(non-homestead) + 6 mills(SET) =24 mills under the new foundation approach.

Third, a portion of the property taxes to support schools is now levied by the State. The State levies a uniform rate of 6 mills on all property — both homestead and non-homestead, with

---

<sup>3</sup> Drawn from: Kearney, C. P. (2001, October). *Michigan school finance*. Unpublished manuscript.

<sup>4</sup> For tax purposes, real property in Michigan is divided into six classes: agricultural, commercial, industrial, timber/cutover, residential, and developmental. Homestead property is a subclass of residential and is limited to owner occupied primary residences. All else — second homes, rentals, and property in the other five classes — is non-homestead.

the proceeds being deposited in the State School Aid Fund and used as a part of State aid under the new foundation approach. Local districts also continue to levy property tax millage. As a result of Proposal A, the maximum allowable millage rate, in general, for school operations levied locally is 18 mills on nonhomestead property. For a district with a millage rate less than 18 mills, the maximum allowable rate is exactly equal to what it was prior to Proposal A. These proceeds constitute the local district's contribution under the new foundation approach.

The state's contribution, the dollars in the School Aid Fund, come from a number of sources but principally the State Sales Tax. With the passage of Proposal A in March of 1994, the State General Sales Tax increased from 4 percent to 6 percent, with the increased revenue earmarked entirely for the School Aid Fund. By prior action, the State Constitution already required that 60 percent of the revenue generated from the existing 4 percent sales tax rate be deposited in the School Aid Fund. Thus, 60 percent of the revenue generated from the first 4 percent tax on general sales, plus 100 percent of the revenue from the additional 2 percent tax on general sales, are constitutionally dedicated to the School Aid Fund.

Even though this is a sizable amount, it does not cover the entire sum needed by the Legislature to fund the School Aid Act. Consequently, other state revenue sources — or portions of them — also are earmarked for the State School Aid Fund. These other sources include revenue from the newly imposed 6 mill State Education Tax, the Income Tax, the Tobacco Tax, the Liquor Tax, the Tax on Commercial and Industrial Facilities, the Lottery, and other miscellaneous taxes. A transfer from the General Fund along with additional state revenues makes up the remaining difference.

#### *Revenue Distribution*

The basic concept undergirding Michigan's new foundation program is that the State will guarantee each district a basic level of funding per pupil provided the district levies a local property tax at a millage rate set by the Legislature. In theory, for 1994-95 the basic level of

funding per pupil, known as the *basic foundation allowance*, was set at \$5,000. In most cases, the maximum allowable millage rate is 18 mills on non-homestead property (as noted above, the State levies an additional 6 mills on both non-homestead and homestead property).<sup>5</sup> Districts did not receive the *basic foundation allowance* of \$5,000 per pupil in 1994-95 but rather an amount, called the *district's foundation allowance*, varying between \$4,200 and \$13,895. However, in order to realize that piece of their foundation above \$6,500, districts had to levy voter approved hold-harmless mills.

These variations in 1994-95 *district foundation allowances* are due to three decisions made by the Legislature. First, rather than move all districts in which the 1993-94 per pupil revenues were under \$5,000 up to \$5,000 immediately, the Legislature chose to move these districts up gradually. Districts below \$4,200 per pupil in 1993-94 were raised to \$4,200 per pupil in 1994-95, or by \$250 per pupil, whichever was greater.

Second, the Legislature chose not to bring all remaining districts up, or down, to a \$5,000 per pupil starting point in 1994-95. Rather, it chose to use each individual district's 1993-94 revenue per pupil level as the starting point and increase that level on a sliding scale. The district in which the 1993-94 revenue per pupil level was closer to \$4,200 received a larger increase for 1994-95 than the district in which the 1993-94 per pupil level was closer to \$6,500.

Third, the Legislature chose not to "level down" but rather to "hold harmless" those districts in which 1993-94 per pupil revenue levels exceeded \$6,500, as long as voters in those districts were willing to tax themselves at a rate in addition to the 18 mill rate.

In addition to receiving a *district foundation allowance*, a local district could levy with voter approval up to 3 additional mills for program *enhancement* in 1994-95, 1995-96, and 1996-97. Beginning in 1997-98, this became *regional enhancement millage* rather than individual

---

<sup>5</sup> Thus, the total tax on homesteads in the district is 6 mills, while the total tax on non-homestead property in the district is 24 mills — 18 levied by the local district plus 6 levied by the State.



district enhancement millage. An intermediate school district (ISD), with the approval of a majority of voters in each district in the ISD, may levy up to 3 mills to enhance local school district operations. The total dollars raised across the ISD are allocated to all of its constituent local districts on an equal per pupil basis. Thus, under *regional enhancement millage*, Michigan has a form of tax base sharing.

### **This Project**

In November 2001, Superintendent of Public Instruction Tom Watkins contacted the North Central Regional Educational Laboratory (NCREL) for assistance in identifying how school funding needs in Michigan have evolved since Proposal A and how the state might respond to these changes. NCREL agreed to fund this study, which seeks to build a consensus across the education, government, and business communities about the school funding issues Michigan should address and how best to work together to resolve these problems. To oversee this project, Superintendent Watkins created an 18-member School Finance Initiative Task Force comprised of faculty members from Michigan State University, the University of Michigan, and Wayne State University, school finance experts from the Citizens Research Council of Michigan and the private sector, and representatives of the Michigan Department of Education. The Task Force met on November 29, 2001, and developed a four-step course of action:

1. Gather state leaders' thinking about the extent and nature of each school funding issue,
2. Analyze these responses in order to identify those issues that a wide range of Michigan policymakers see a need to address,
3. Lay out effective options for school finance mechanisms and structures that can serve this consensus, and
4. Recognize that the choice among these various effective options resides with state leaders.

The Task Force explicitly decided that it would not seek to develop a comprehensive school finance reform package that it could propose on the basis of previously held theoretical or hypothetical considerations. Instead, the Task Force decided its most productive role would be to outline a broad range of options focused on achieving the objectives identified by state leaders.

### **Interview Procedures**

The initial step in this project was gathering critical information from Michigan's leaders about the definition and nature of the state's school funding problems, as well as possible solutions. During January 2002, Neil Theobald, Associate Professor of Educational Finance at Indiana University and Immediate Past President of the American Education Finance Association, conducted 30 in-person and three telephone interviews with a variety of stakeholders including the legislative leadership, members of the executive branch, the Michigan State Board of Education, the Michigan Education Alliance, and public school educators. The Appendix to this report lists those interviewed.

These interviews asked five sets of questions:

- What do you perceive to be the strengths of Michigan's system of school finance?
- What do you perceive to be the weaknesses or flaws in Michigan's system of school finance?
- What do you see as the 3-5 most important problems to be resolved or goals to be achieved by Michigan's system of school finance? For each problem or goal, how well does Michigan's system of school finance address this problem or goal? If you judge that Michigan's system of school finance doesn't address this goal well, what could be done to improve the system?
- In addition to school finance goals, are there other statewide problems or goals that this review should take into consideration? For each problem or goal, does Michigan's system of school finance facilitate or impede the state in resolving this problem or meeting this

goal? If Michigan's system of school finance impedes the state, what could be done to improve it?

- The 1994 adoption of Proposal A and related legislative actions sought to create (a) an adequate revenue stream, (b) equity for taxpayers, (c) equity for pupils, (d) choice at the parent, pupil, school, and district level, (e) efficiency/accountability, and (f) a balance among equity, choice, and efficiency. How successful has Michigan been in creating each of these conditions?

### **Interview Responses**

These 33 interviews suggest that four issues dominate school finance discussions in Michigan (ordered by number of individuals mentioning each issue):

- School construction/infrastructure funding
- Administrative costs
- Access to local millage
- Declining enrollment school districts

In addition, low-performing schools and special education were mentioned by a significant number of the individuals interviewed. Within the last year, the State Board of Education has developed and implemented wide-ranging policies with regard to both of these issues. Therefore, in order to avoid duplication of effort, neither of these issues will be further analyzed in this report.

Clearly, other observers of the Michigan school funding scene may differ with the issues identified by these 33 stakeholders. Following the issuance of this report, individuals with alternative views will have the opportunity in regional forums to discuss — and seek to modify — the issues under consideration. For the purposes of this project, though, it is important to recognize that political discourse at a state level necessarily involves those topics that compete most successfully for attention on the public's agenda. Thus, the success of any attempt to

improve the quality of decisions made about Michigan's system for funding public schools must be inclusive of, and indeed must be driven by, these widely-shared issue and problem formulations.

Before describing each issue, it is important to note the unanimous support given to Proposal A in these interviews. The interviewer has conducted in-depth analyses of the school finance systems in four other states (Indiana, Iowa, Ohio, and Washington). In none of these four states did the views of a cross-section of leaders approach the unanimous support provided to Proposal A by the 32 informants in Michigan. Thus, it is crucial in what follows to ensure that any changes proposed do not undermine the substantial gains the state has made since 1994 in lowering property taxes and improving the stability, adequacy, and equity of the revenue distribution system.

#### *School Construction/Infrastructure Funding*

Proposal A addressed the distribution of operating revenues only and kept capital funding as a local responsibility. Clearly, property values are unequally distributed around Michigan as they are around every state. This provides some districts with greater capacity to raise funds for local building projects than is available to other districts. Everyone who was interviewed agrees on these basic points. Unfortunately, the consensus stops here.

The views expressed range from those who prefer that the current system remain unchanged (i.e., local control over facilities, reliance on local property taxes) to those who would abolish local school districts and set-up a statewide facility manager. Between these views are a significant number of interviewees who would like to see the state subsidize these costs for low-wealth districts, several individuals who would like to see more intergovernmental sharing of facilities among schools, cities, and park districts, those who see school consolidation as a promising avenue, and individuals who would establish a Proposal A-like system for equalizing capital funding across all Michigan school districts. Repeatedly, the goal was stated that nothing

should be done that would “treat unfairly those districts that have passed bond issues and already taxed themselves for new schools.” Any proposed change must address the widely stated concern “that those districts who would get a state bail-out are those who have not maintained their facilities; those who have raised taxes in the past will get nothing. That’s not fair and would raise the bar mightily for ever passing a bond issue again.”

### *Administrative Costs*

The cost and complexity associated with managing school districts in Michigan has increased significantly during the past decade. Competitive pressures introduced by choice options and constituent demands for services have broadened the responsibilities undertaken by K-12 districts in Michigan. Given the wide variety of districts in Michigan, and significant differences in the cost of operating them, it is not surprising that state leaders place significant emphasis on ensuring the efficient use of resources.

The main objectives expressed in the interviews include:

- Providing administrative services more cost effectively;
- Establishing more collaborative and integrated cross-district sharing of administrative services; and
- Reorganizing administrative structures to better leverage the state’s investments in information technology, including the Standard and Poor’s data system.

State leaders recognize that significant efforts in this regard “are already going on. ISD [Intermediate School District] coops buy copiers and paper and provide special ed. and vocational ed. We need to look at adding things like payroll, accounting, and computer services, though.” As this comment suggests, the primary focus is on finding ways to streamline the business side of school operations. Another leader suggests, “We need to have clear financial performance standards, including specifics on district level fund balances as well as suggested ‘benchmarks’ for all areas of operations.”

Not surprisingly, given the labor-intensive nature of K-12 education, several informants focused on controlling costs. “Michigan has extraordinary benefits costs for education employees. We need to get the ‘ownership of the policy’ back in the hands of districts or ISDs so they have the ability to shop around for insurance.”

It is important to recognize that although all districts are part of the Michigan system of public schools, each district faces a distinct and different set of challenges. For example, school districts have different types of students who live in different regions of the state. The relative isolation faced by the districts in the Upper Peninsula was mentioned often as a challenge that the state must consider as it determines a practical implementation path for these cost savings opportunities.

#### *Access to Local Millage*

The individuals interviewed for this study criticized the property tax as a source of revenue for education. The criticisms centered on two features. First, the property tax, because of its focus on the value of real property holdings, is based only on a partial measure of taxpayers’ ability to pay. Two taxpayers may have the same overall capacity to pay taxes, but could find themselves paying different amounts of property tax depending on the degree to which their fiscal wherewithal takes the form of real property. The example raised most often in this regard is when elderly taxpayers on limited fixed incomes find themselves paying large property taxes because they continue to own valuable homes that were purchased in the distant past. Proposal A is given a great deal of credit for lessening this problem in Michigan.

Second, the property tax was blamed for wide differences in school district’s ability to raise the same amount of money with the same tax effort. It should be recognized, though, that this variation is based on the tendency for wealth, regardless of how it is measured, to be distributed unevenly across geographic regions. Variation in the wealth of school districts does not occur because of reliance on the property tax; this variation would exist to some degree

regardless of what local tax is used to finance education. Nevertheless, the property tax facilitates the use of local sources of revenue for education and thereby plays a role in the formation of a schooling system characterized by substantial amounts of fiscal inequality from one district to the next.

Despite these shortcomings, the results of the interviews suggest that there is some support for “more locally preferred levels of program provision.” The primary concern expressed with the present system is that there is “virtually no ability to use locally-raised resources to support local enhancements.”

Unfortunately, as one informant stated, “there’s not much middle ground” on expanding access to local millage. A sizable portion of those interviewed stated positions consistent with “local option should be avoided like plague; as the death of the equity gains of A. . . . Issue here is whether or not we plant the seed that destroys all of A’s equity gains.” The concern is that more flexible access to local effort “would allow high revenue districts to pull away from equity. Allowing individual districts to pass millage would break promises made in 1994.” For many of those interviewed, “This is not an issue.” Even those who believe ‘this is an issue’ are pessimistic that change is forthcoming, “More flexibility is needed but it will be seen as a tax increase [by state legislators] so it won’t happen.”

### *Declining Enrollment School Districts*

State leaders make an important distinction between two types of declining enrollment school districts. Those districts that are declining in enrollment because parents choose to move their children to other school districts (i.e., “choice-driven enrollment decline”) are not seen as a significant issue to be addressed in this report. Districts that are declining in enrollment, though, because “more people are dying in the community than are being born” (i.e., “demographically-driven enrollment decline”) — several school districts in the Upper Peninsula and former

manufacturing centers were specifically cited — are seen as “a good area for the State Board of Education to float proposals of what the state should do.”

All states have school districts with demographically-driven enrollment decline and Michigan has had them for years. Proposal A, though, brought this issue to the forefront because it funds school districts on a per-pupil basis and “put focus on attracting students.” Supporters of transitional funding note that demographically driven declining enrollment districts “tend to have less than 1,000 students and have substantial fixed transportation and heating costs. The parents in these districts have no options to go elsewhere [because of relative isolation]. I don’t understand why there is such unwillingness to address this issue because it would cost the state very little.”

Those who oppose such funding argue, “The danger here is moving back to categorical programs. They take money away from all kids. The State Board needs to be a strong voice for increasing general aid and leaving decisions to districts.” Another leader adds simply, “The legislature does not want to move back to categorical funding.” Thus, a K-12 educator concludes, “The reality is that chances of this passing are slim-to-none. The last thing legislators want to do is go back to the old system.”

### **Options**

This section outlines a wide range of options for addressing the issues discussed in the previous section:

- School construction/infrastructure funding
- Administrative costs
- Access to local millage
- Declining enrollment school districts

Each series of options is organized to first discuss marginal changes to existing practice with more substantive changes outlined in the latter part of each set of options.



### *School Construction/Infrastructure Funding*

School construction and other capital funding has been a local responsibility in Michigan for over 150 years. One option available to the state is clearly to maintain local responsibility for school buildings and infrastructure. Alternatively, the state could conclude that while local funding of capital has worked well in many districts, it doesn't work well in all cases — the state should become more involved in school construction/infrastructure funding. In February 2002 the Senate Republican Caucus proposed that the state subsidize school infrastructure needs by offering interest-free loans to lower school construction borrowing costs for property-poor school districts.

A more dramatic form of state involvement would be for the state to take the position that some Michigan school districts, through no fault of their own, lack the property base to maintain and replace their buildings. To remedy this situation, the state could choose to create a capital funding partnership at the state level that mirrors the partnership that currently exists on the operating side or, more intrusively, the state could dissolve these school districts and consolidate them into neighboring districts. At an extreme, the state could address this issue by assuming total responsibility for funding, or even operating, the state's public schools.

#### *No State Action*

##### *Option 1: Continue with the current capital funding process.*

Those who oppose state involvement in capital funding do so primarily for two reasons. First, they worry that those districts that have previously taxed themselves for school construction and infrastructure will not be treated fairly and the state will “bail out” those districts that have not raised taxes in the past. Second, they foresee negative consequences in minimizing or disconnecting local tax effort from these expensive projects. These individuals believe that the adequacy of an existing building is highly subjective. While newer structures may be championed, they point out that older buildings that are clean, well maintained, and often

located in the center of communities can actually be preferred by the community. They further argue that newer buildings that are not well maintained can quickly become inadequate. A key issue for these individuals is that the adequacy of school facilities is not simply a financial issue. They worry that if the local community is not required to pay the full cost of school construction: (1) schools will choose to build more expensive structures than are actually required, and (2) local commitment to maintaining these structures will lessen.

#### *State Subsidy*

*Option 2: Issue state bonds, or use other techniques, to subsidize interest rates for school districts.*

Legislation has been introduced in the Michigan Senate to issue a \$1 billion General Obligation bond to create a pool of state funding that could be used to lower the costs of borrowing for infrastructure needs. Under this proposal, school districts passing bond issues after June 1 would be eligible to borrow all or a portion of the total bond from the State at zero interest rate. The amount of the total bond issue that could be borrowed at the zero interest rate would depend on the property wealth of the school district. This proposal must be approved by two-thirds vote of both chambers of the Michigan Legislature to be considered by voters on the November 5 general election.

#### *Option 3: Improve School Bond Loan Fund.*

Other observers believe that the state could assist a broader range of school districts by funneling any new appropriations into the existing School Bond Loan Fund. More than 100 school districts currently borrow from the Michigan School Bond Loan Program to meet annual payments to retire debt on building projects.

#### *Option 4: State grants for capital construction.*

Other observers call for on-going subsidy of school building/infrastructure costs. The views expressed were not uniform, though. Some thought that the state should simply “divert a

portion — let's say half a mill — of the required six mills to capital.” Others called for “an additional statewide one-mill levy and that would be shared on an additional revenue/pupil basis.” Those supporting state assistance see the “key is how to treat fairly those districts that have passed bond issues and not give all the dollars to those who have not.” The mechanism of choice for these individuals is to distribute any state funding inversely to State Equalized Valuation Per Pupil (SEV).

*Option 5: Guaranteed per-pupil allotments for capital construction.*

Other options include establishing a minimum per pupil guarantee for capital needs — secondary students would be guaranteed more capital funding per pupil than elementary students — for low SEV per pupil districts. In such a system an amount based on each district's SEV would be subtracted from this guarantee in order to provide equalization across these districts. Broader steps include “a Prop A-like system with minimal local property taxes and a state property tax for financing.”

*State Administrative Action*

*Option 6: Establish a state property tax control board.*

Currently, unlimited qualified bonds must be approved by the Superintendent of Public Instruction and are guaranteed 100% by the State.<sup>6</sup> An intermediate role that the state was urged to play is extending such review to all local capital project financing decisions. Rather than second-guessing these plans, the goals of such a state board would be to ensure that enrollment projections used to justify the project are accurate and less costly alternatives are examined and, if they are rejected, such action is taken for valid reasons.

---

<sup>6</sup> For further details, see Addonizio, M. F., Madigan Mills, E., & Kearney, C. P. (2001). Michigan public school finance program. In C. C. Sielke, J. Dayton, C. T. Holmes, & A. L. Jefferson (Eds.), *Public school finance programs of the United States and Canada: 1998-99* (pp. 1-30). Washington, DC: U. S. Department of Education, National Center for Education Statistics (NCES Publication 2001-309).

*Option 7: Encourage school districts to lease, rather than own, buildings.*

A specific alternative that was mentioned is urging districts to move from owning buildings to leasing them. The argument centered on the ability of private developers to build the structures at a lower initial cost and included the idea that because the district would lease these buildings for a fixed time only, they could be built so they can more easily be converted to other uses (e.g., senior centers) as the population ages. This approach has been considered by several school districts across the nation. Before the state moves to broaden such efforts, it should evaluate the leasing experiences of these districts.

*Option 8: Fund capital construction on an ISD-wide basis.*

One approach to reducing inequities across districts in the ability to raise funds is to require school districts to fund capital construction on a regional basis. This option would require all school districts in an ISD to impose a common rate of tax on their properties, in contrast to the current practice of allowing individual school districts to impose different rates of property tax on properties located only within their own single district. The revenues raised regionally from the common rate of tax would then be distributed back to the districts in an equalizing fashion. One advantage of the regional approach is that individual districts are less able to benefit from the location of highly valuable individual pieces of property such as shopping centers or utility plants. One disadvantage is that voters who accept the drawbacks from living near a shopping center or utility plant would be required to share the benefits of this valuable property.

*Option 9: Commission standard building designs to be used by all Michigan school districts.*

Standardizing school building design is seen as decreasing planning and construction costs. School districts would have a limited number of options from which to choose, but proponents believe they could substantially lower construction costs by allowing contractors to generate significant economies of scale by building to a standard design.

*Option 10: Consolidate school districts to better match capital needs with available buildings.*

Michigan clearly has a strong tradition of local control of schools, although continued support for such decentralized decision-making is far from universal. With regard to school construction, the crux of this disagreement is the sanctity of existing district boundaries. A majority of those interviewed held positions that are consistent with the one legislator's view that "if the state is to provide funding for construction, it must have some say over district boundaries and district size." A sizable group believes that "changes in arbitrary district boundaries" (i.e., school district consolidation) is a necessary and sufficient solution to addressing capital inequities. Yet, several legislators warned that mandating such changes would be politically difficult.

#### *Direct State Funding*

*Option 11: Eliminate local funding of capital construction.*

Among the more ambitious plans was a call for eliminating local school construction bonding, with the state providing all capital funds. A more radical version of this proposal would abolish school districts and transfer all buildings to the state, which would act as facility manager. The goal would be to more flexibly use the existing stock of buildings. New buildings and renovations would be provided from state funds as this existing stock proved inadequate. To return to a finding emphasized earlier, either of these two systems is likely to attract a firestorm of criticism for, among other things, unfairly treating voters who previously taxed themselves to meet minimum standards for school facilities.

#### *Administrative Costs*

The guiding principles in what follows are not unlike those set forth by other states seeking to improve the efficiency of their administrative functions. The common denominators in each option are the increased use of technology and new business practices or processes. A

senior member of the legislative leadership suggests that the State Board commission further study to learn from other states that have expanded upon the shared administrative services currently provided by the state's 57 regional educational service agencies (ISDs). The goals of these efforts should be to identify opportunities to achieve further cost savings, cost avoidance, and/or improvement in the delivery of administrative services.

Due to limited time and resources, this project addressed only the first phase of the work necessary to identify administrative cost savings. The observations that follow are based solely on the 33 interviews and can evaluate, at a high level only, the administrative functions that should be evaluated in greater depth during a second phase. The criteria used for selecting these administrative functions include an assessment, based on the author's previous K-12 administrative experience, of those functions that would provide the greatest likelihood for administrative cost savings or cost avoidance. Failure to include a function should not suggest it is deemed to be operating without the potential for improvement. The State Board of Education might consider establishing an ongoing and iterative process to identify further opportunities for administrative efficiency in the future.

### *Benchmarks*

*Option 1: Design and implement a formal performance assessment process to ensure that administrative functions meet the needs of the schools they support.*

Several state leaders called for the development of 'benchmarks' for districts to use in evaluating the effectiveness of their administrative services. One approach to developing such benchmarks would be for each school district administrative department to conduct a customer needs assessment and then develop metrics. The district could then monitor the department's performance against these benchmarks.

The school business administration literature provides numerous approaches for conducting such customer needs assessments.<sup>7</sup> The stages of a well-established process are:

- Identify the schools' specific needs for products and services and their current satisfaction with these services.
- Compare current performance with the desired performance level.
- Create a prioritized plan to close the gap between the current and desired future state.

Each administrative department should determine the appropriate metrics to measure its performance. For example, a personnel department should include the average cost per hire, the average quality of new hires as measured by school principals, and turnover costs. According to the reasoning underlying this process, if each administrative department is measured against agreed upon metrics, it will more than likely improve its efficiency, effectiveness, and ultimately lower the cost of providing these administrative services.

*Option 2: Analyze state-imposed administrative costs to ensure that they are cost-effective.*

School districts are not able to unilaterally set their administrative structures. They must employ staff to implement and coordinate mandated program requirements. Observers recommend that the State Board review such program requirements to ensure that the administrative cost that school districts incur are justified by the services provided.

#### *Cross-District Coordination of Administrative Services*

*Option 3: Increase the consistent use of a cross-district preferred vendor programs.*

While Michigan's ISDs operate purchasing cooperatives for bulk items, the purchasing functions within school districts have historically operated independently. Purchased goods and services approach \$1 billion statewide and there are a limited number of preferred vendor

---

<sup>7</sup> See, for example, Ray, J. R., Hack, W. G., & Candoli, I. C. (2001). *School business administration: A planning approach*. Boston: Allyn & Bacon.

agreements.<sup>8</sup> Those agreements that do exist are offered by vendors to each district or ISD, but are not negotiated on the basis of the state's collective buying power. As a result, the agreements do not achieve the lowest cost or best service available. Using a large number of vendors also increases accounts payable transaction costs. Even with ISD-wide contracts in place, districts are not required to use the specified vendor. State encouragement/mandate that school districts expand the use of preferred vendor agreements should lower prices and decrease processing time, resulting in further cost savings. Computers, and other high-priced, mass-produced items, should be particular targets for such preferred vendor agreements.

*Option 4: Expand cross-district personnel service centers that are responsible for transaction processing.*

Some ISDs currently offer centralized payroll and related services. The state could expand these cross-district service centers to include all transaction related services that are not 'employee facing' such as benefits enrollment processing and data entry. Under such a model, employees would still have local access 'employee facing' personnel services. However, by centralizing certain administrative functions, district-based personnel representatives would have more time to focus on issues that are truly unique to that district. Some district-specific issues include performance counseling and employee questions regarding payroll and benefits.

*Option 5: Maximize the potential of ISDs to become administrative services organizations.*

ISDs currently provide a wide range of administrative services. The potential exists for them to expand dramatically upon this base and assume much of the macro side of management during operated independently by each school district. Examples of large scale functions that ISDs might assume are purchasing, payroll, benefits, accounting, transportation, and recruiting. Centralizing these roles at the ISD level would allow school districts to focus on instruction.

---

<sup>8</sup> A widespread exception to this statement is the presence of single-vendor soda machines in many school districts.



## *Market-Based Approaches*

*Option 6: Distribute revenues to school level and let school choose from whom to purchase services.*

A perception exists that the schools, which are the purpose for which the district exists, don't have enough control over the way administrative units are managing their operations. As a result, one informant concludes, "Although the general philosophy of providing central office support services should be maintained, there may be areas in which fee-for-service arrangements are appropriate." Implementation of such an option in the current district structure is complex. Issues such as the loss of economies of scale in essential services and the lack of genuine alternatives for the user could constrain progress. In addition, building-level budgeting would involve building principals in a range of activities that could reduce the time they have available for instructional support and direction.

*Option 7: Privatize school business operations.*

Decentralized, building-level financial decision-making could be facilitated by making available a variety of genuine alternatives for purchasing central office services. One approach to providing such choice would be to provide school district business offices with a set number of years to transition into market-based entities. At that time, schools would be free to enter into fee-for-service arrangements with any provider.

## *Legislative Changes*

*Option 8: Refocus ISDs from regulatory to administrative functions.*

A number of Michigan statutes currently require ISDs to play a regulatory role with local school districts. Centralizing this regulatory function at the state level could provide free ISDs to generate cost savings for the state by providing substantially more cross-district coordination of administrative services.

### *Access to Local Millage*

The opposition voiced in the interviews to providing more flexible access to local millage deals mostly with the impact of local variation in wealth as well to local variation in willingness to approve higher millage rates. It is clear that Michigan's state leaders are determined to use the state's school funding formula to reduce inequities across districts in the ability to raise funds.

Fortunately, options do exist to address these problems. In contrast to the traditional practice of allowing individual school districts to impose different rates of property tax on properties located only within a single district, Michigan currently allows school districts in an ISD to impose up to 3 mills of additional local effort on all properties located in an ISD. The revenues raised regionally from the common rate of tax are then distributed back to the districts on a per-pupil basis. One advantage of this ISD-wide approach is that individual districts are less able to benefit from the location of highly valuable individual pieces of property such as shopping centers or utility plants. However, as one senior senator pointed out, "voters will be less likely to want a factory in their back yard if they can't get the benefit of the added tax base."

#### *Voting Changes*

*Option 1: Simplify the mechanism for approving the 3-mill levies by requiring majority approval at the ISD level rather than majority approval in each LEA.*

Only one ISD has raised a 3-mill levy. Critics cite the need to receive majority approval in each district as an unrealistic standard. For these individuals, the proper unit of approval is the ISD. If the majority of voters who are to be taxed approve, then a minority of voters who happen to live in one district should not be able to block the levy. Those in favor of the status quo reply that the voters in each school district should control their own property tax rates. A specific fear is that voters in small districts would be disenfranchised by a move to count votes at the ISD level.

*Option 2: Allow a subset of districts in an ISD to seek approval for a 3-mill levy.*

Another approach to increasing the capacity of individual districts to access the 3-mill levy would be eliminating the all-or-nothing requirement that each district in an ISD participate. Only those districts that chose to seek the levy would vote and only their tax rates would be affected. A variant of this proposal would be to hold ISD-wide elections as currently, but allow the levy in only those districts in which a majority votes in favor. All revenue would be shared on a per-pupil basis among those districts approving the levy.

*Option 3: As the State Board establishes some “probation-like” status for poor academic performance; allow these districts to seek local levies.*

An exception to the strong support for requiring ISD-wide or other regional pooling of local effort is in the eventuality that a school district is identified as a poor performer. Several informants believe the state should allow these districts to seek additional local millage to fund remediation and other program enhancements.

*Option 4: Allow individual districts to pass the 3-mill levy but apply it to homesteads only.*

Applying the current process, or any of the proposals outlined above, to homesteads only would “better match those who vote with those who pay.” Depending on the extent to which homestead values vary across districts, it is likely that it would be necessary to pool these revenues across the ISD, region, or state to provide more equal funds.

#### *Redistribution*

*Option 5: Pool the revenue generated by all 3 mill levies that are passed in Michigan and divide it on an equal per pupil basis among all districts that pass levies.*

This option would guarantee that 3 mills of property tax effort provides the same amount of money per pupil for every school district in Michigan that chooses to approve higher millage

rates. As pointed out earlier, critics believe that such a proposal would be unfair to those who live with the drawbacks of having “a factory in their back yard.”

*Option 6: Pool a portion (e.g., 70%) of the revenue generated by all 3 mill levies that are passed in Michigan and divide this portion on an equal per pupil basis among all districts that pass levies. The remaining levy revenue is retained at the local school district level.*

In order to address the concerns that taxpayers who live with the drawbacks of having “a factory in their back yard” should receive some of the benefits, this option would allow high-wealth districts to retain some of the revenue by their larger tax base. At the same time, though, it would provide other districts with access to a portion of this tax base.

#### *Declining Enrollment School Districts*

The Michigan school funding formula generates an equal per-pupil grant to all regular education students who are residents in a particular school corporation. Thus, revenue is tied directly to enrollment changes. School districts can fairly easily — at least over a reasonable period of time — respond to enrollment increases (and the accompanying revenue increases) by employing more teachers and operating more buildings.

The cost savings that a school corporation can realize when its enrollment falls, though, differ substantially by the degree to which the corporation is able to realize these savings by employing fewer staff or operating fewer buildings. Factors that can dull school district responsiveness include continuing contract requirements for employees and the number of buildings being operated. Clearly, a one-building district would have little flexibility in closing schools.

The term often used for the cost structure of school districts is that they are “sticky downward.” In other words, it is far more difficult for them to shed teachers and buildings as enrollments decline than it is for them to add teachers and buildings and enrollment grow. While a senior legislator observes that the issue of declining enrollment school districts “has not caught

a lot of fire”, other observers argue that “older school districts that are losing enrollment while facing static fixed costs need help.”

*Option 1: Adjust the current 80/20 weighting of school district enrollment to a more even distribution.*

Michigan already addresses the issue of declining enrollment by calculating per pupil funding on a weighted average of last February’s enrollment (20%) and this September’s enrollment (80%). Adjusting this weighting to emphasize last year’s enrollment would clearly benefit declining enrollment districts. As currently structured, though, this is a zero-sum approach that would shift revenue away from increasing enrollment districts that must hire additional staff, purchase additional equipment, and so on.

*Option 2: In the school funding formula, weight students in demographically-driven declining enrollment school districts more heavily (i.e., provide more than \$6,500).*

A number of states use an adjustment for sparsity in their school funding formula. In other words, children in remote school districts are provided more per-pupil funding than are children in less sparsely populated regions of the state. In a similar manner, Michigan could establish a definition for demographically-driven declining enrollment school districts and provide children in these school districts with more per-pupil funding than is provided elsewhere in the state. One possibility is to require these districts to meet two criteria: (1) declining population, and (2) declining number of occupied dwellings.

*Option 3: Allow declining-enrollment districts to phase-in these reductions over a five-year period.*

Several observers see the “lack of a guaranteed provision for declining enrollment to be the greatest weakness in the current formula.” For school districts with declining enrollment, they would suggest that funding for lost students be phased-out over five years. For example, the lost pupil is funded at 80% in the first year after the student is lost, 60% the second, 40% the

third, 20% the fourth, and at 0% thereafter. This will allow these districts to “shrink gracefully and use voluntary attrition to cut their staff.”

*Option 4: Allow declining enrollment districts to seek local levies.*

Under this proposal, individual declining enrollment districts that lose a given percentage of students would be authorized to seek approval of an additional levy to help cover costs that do not vary substantially by student enrollment (i.e., utilities).

*Option 5: The State should encourage rural districts in the Upper Peninsula to work with Michigan Tech, Northern Michigan, Lake Superior State, and other Michigan colleges and universities for distance education instruction.*

Expanded use of distance education for students in remote areas of Michigan could allow these districts to educate high school students in a more cost-efficient manner.

*Option 6: The State should reorganize some school districts by either forcing consolidation.*

Several observers point to school districts with substantial declining enrollment that could be “dissolved” and merged into neighboring districts. Other leaders, though, commented, “the political implications of forced consolidations would be very significant.”

## **Conclusions**

By seeking to identify common goals for a state’s system of school funding, this project is attempting to provide an objective, non-partisan basis for the logical next step, which is to determine specific funding proposals that lead to the achievement of the goals that make up this agenda. This process is designed to shield decision-makers from being rushed prematurely towards crafting solutions. Instead, it allows policymakers to undertake the systematic analysis and deliberation needed to understand the nature of the challenges facing them and to reach agreement about how to make progress in overcoming these challenges.

At least two caveats must be considered. First, it must be recognized that the information generated by this project will be used in the larger political context of a state legislature. A dominant view in policy research is that policymakers fasten upon information that affirms their convictions and use it to advance their goals and preferences.<sup>9</sup> This report does not attempt to substitute information for politics. Instead, it attempts to integrate politics into the information-generating process by seeking to ascertain points of consensus among policymakers and interest groups regarding key pieces of the debate over how best to finance Michigan's schools.

Second, it is possible for individual points of consensus to be inconsistent with one another. Experience suggests that so long as the debate is highly abstract, it is relatively easy to “paper-over” differences in points of view with lofty rhetoric. However, when attention turns to the design and implementation of real world policy, the ability to finesse underlying differences in the point of view can decline, and disagreements can become quite sharp.

The process outlined in this paper has evolved since 1994 to recognize and attempt to address these realities. Central to our evolving understanding of state school funding is that no definitive solution exists for the funding questions in any state. The lack of a definitive answer, though, does not preclude deducing on principled grounds a viable direction in which to proceed.

---

<sup>9</sup> This phenomenon is not unique to policymakers. For a readable account, see Gilovich, T. (1991). *How we know what isn't so: The fallibility of human reason in everyday life*. New York: Free Press. For a scholarly review, see MacCoun, R. J. (1998). Biases in the interpretation and use of research results. *Annual Review of Psychology*, 49, 259-287.

## Appendix

The task force would like to thank the following individuals for generously taking time from their busy workdays to provide me with the insights and observations that form the knowledge base for this report:

Michael Addonizio  
Associate Professor  
Wayne State University

John Austin  
Member  
State Board of Education

Jim Ballard  
Executive Director  
Michigan Association of Secondary School Principals

A. Thomas Clay, Jr.  
Senior Research Associate  
Citizens Research Council of Michigan

Julie Cullen  
Assistant Professor  
University of Michigan

Laurie Cummings  
School Aid  
House Fiscal Agency

Senator Dan L. DeGrow  
Majority Leader  
Michigan Senate

Douglas Drake  
Associate Director, State Policy Center  
Wayne State University

Senator Harry Gast, Jr.  
Chair  
Senate Appropriations

Todd Harcek  
Staff  
House Appropriations Committee



Bob Harris  
Public Education Advocate  
Michigan Education Association

Ellen Hoekstra  
Lobbyist  
Michigan Federation of Teachers and School Related Personnel

Representative Ronald Jelinek  
Chair  
House Appropriations Subcommittee on School Aid/Department of Education,

Scott Jenkins  
Education Policy Advisor, State Government Affairs  
Governor's Office

C. Philip Kearney  
Professor Emeritus  
University of Michigan

Representative Wayne Kuipers  
Chair  
House Education Committee

Eileen Lappin Weiser  
Treasurer  
State Board of Education

Gary S. Olson  
Director  
Senate Fiscal Agency

Glenn Oxender  
Superintendent  
Mendon Community Schools

David Plank  
Director, Education Policy Center  
Michigan State University

Hank Prince  
Associate Director  
House Fiscal Agency

Dan Quisenberry  
President  
Michigan Association of Public School Academies

Earl M. Ryan  
Executive Director  
Citizens Research Council of Michigan

Jim Sandy  
Director  
Michigan Business Leaders for Educational Excellence

David Seitz  
Staff for Speaker Rick Johnson  
Michigan House of Representatives

Al Short  
Director of Government Affairs  
Michigan Education Association

Senator Leon Stille  
Chair  
Senate Appropriations Subcommittee on School Aid/Department of Education

Kathleen Straus  
President  
State Board of Education

Richard Studley  
Senior Vice President, Government Relations  
Michigan Chamber of Commerce

Roger Swaim  
Legislative Liaison  
Michigan Elementary & Middle School Principals Association

Ray Telman  
Executive Director  
Middle Cities Education Association

Glen Walstra  
Executive Director  
Michigan Association of Nonpublic Schools

Michael David Warren, Jr.  
Secretary  
State Board of Education